No. 10203

IN THE UNITED STATES CIRCUIT COURT OF APPEALS

For the Ninth Circuit

APARTMENT OPERATORS ASSOCIATION,
a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S REPLY BRIEF

EDWARDS MERGES,
JOSIAH THOMAS, AND
CLARENCE L. GERE,
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ARGUMENT

The Courts have ruled construing Treasury Regulations in accordance with contention of Petitioner, that *it is a business league.*

Respondent's answering brief seems to readily admit that the facts are as stated by petitioner in its opening brief, which includes that on the face of the record and under the findings of the Trial Examiner, the only net increase in the income for the year 1938 was $356.35. This is a proceeding in equity and this

Court is empowered to do equity; whether or not every detail of the points relied on checks with the ideas of counsel for respondent. However, these things are mentioned for the purpose of leading to the one and apparently only controverted issue, and that is, what is the test of a business league? Putting it in another way: "is the test *determined* by what respondent *claims* is the *Treasury regulation* (as he sets forth in his brief at the bottom of page 16, and his deductions therefrom), or is it determined by what the *Courts* have *ruled* in regard to Treasury regulations?" Petitioner relies upon what the Courts have heretofore said, and cites the case of *American Society of Cinematographers, Inc., petitioner, vs. Commissioner of Internal Revenue*, 42 B.T.A., 675, as pertinent to the present inquiry.

In that case the petitioner was a non-profit corporation organized under the laws of the State of California. It had no capital stock and no dividends or profits were ever distributed to members. The object of the corporation was, among other things, to bring cinematographers together in order that there might be an 'interchange of ideas and experiences.' The corporation was authorized to own and hold property. Dues were paid by members and a monthly magazine was published. The petitioner represented its members in labor negotiations and had an 'emergency fund' out of which death benefits were paid. The only question presented was whether or not petitioner was exempt

under Sec. 101, Revenue Act of 1934. One of the principal arguments of the respondent there was that the petitioner should not be exempt because it published a magazine. It was held that the petitioner was exempt, and the opinion read, in part, as follows, page 679:

> "The evidence shows that this magazine was at its inception an organ for the dissemination of scientific information to its members. * * * The magazine is concerned exclusively with the publication of articles which are of assistance to its members and to news throughout the world. It was never expected that the magazine would be operated at a profit to the membership. * * *
>
> "The courts have uniformly held that the destination of income rather than the source is the ultimate test of exemption. See Trinidad vs. Sagrada Orden De Predicadores, 263 U. S. 578. In that case the collector claimed that a religious corporation had lost its exempt status because it owned and operated large properties in the Philippines consisting of real estate and stocks in private corporations and loaned money at interest. The Supreme Court held, however, that the corporation was operated exclusively for religious purposes and that it did not lose its exempt status because it realized profits from certain enterprises which were devoted to the objects of the order. *The destination of income was held to be the factor of prime importance.* (Italics ours.)"

It will be noted that in the instant case, the purpose of the Journal or Magazine published by petitioner, was to disseminate information among its members and to allow an exchange of ideas.

As found by the Trial Examiner (Tr. 102) and cited in Petitioner's Opening Brief, p. 5:

> "Petitioner has no purpose or intention of making a profit, but it tries to have a small surplus to assure its continuance."

The case of *Trinidad vs. Sagrada Orden,* supra, gives full answer to the respondent's contention that the articles of merchandise handled by the petitioner places it in the class of a profit making corporation. Since the court is undoubtedly familiar with the facts involved in the *Trinidad* case, supra, it will be unnecessary to restate them here. Suffice it to say that the plaintiff corporation in that case was devoted to religious and charitable work but dealt in certain commodities the profits from which were used in furthering the work of the corporation. In holding the corporation exempt, the court said:

> "As respects the transactions in wine, chocolate and other articles, we think they do not amount to engaging in trade in any proper sense of the term. It is not claimed that there is any selling to the public or in competition with others. The articles are merely bought and supplied for use within the plaintiff's own organization and agencies—some of them for strictly religious use and others for uses which are purely incidental to the work which the plaintiff is carrying on. That the transactions yield some profit is in the circumstances a negligible factor. Financial gain is not the end to which they are directed."

The *Trinidad* case, supra, has been consistently followed by the courts. One of the latest cases in which it was cited is that of *Koon Kreek Klub vs. Thomas,* 108 F. (2) 616. In that case the petitioner was a private fishing and hunting club. This club, however, leased

certain of its lands for money, devoting the proceeds to the purpose of providing hunting and fishing facilities to its members. In holding the club exempt the court said:

> "We think the question is controlled by the decision in Trinidad vs. Sagrada Orden, 263 U. S. 578, * * * wherein the Court points out that the statutes say nothing about the source of the income but makes its destination the ultimate test of exemption. * * * "

The case of *Chicago Graphic Arts Federation, Inc., vs. Commissioner,* Docket No. 97569, entered November 8, 1940, (C.C.H. 11, 380 A) is very similar to the instant case. In that case the petitioner was a non-profit corporation organized under the laws of Illinois. The purpose of the corporation, as set forth in its articles, was, in substance, to promote the welfare of the printing industry by cooperation and dissemination of information among its members. The corporation had an operating personnel consisting of a secretary and others who received salaries, and it maintained offices. There was no capital stock and no dividends were distributed, such being prohibited by the laws under which the corporation was organized, just as in the instant case. The corporation, just as in the instant case, supplied credit information to its members and among other things conducted a waste paper bureau for members wishing to sell waste paper, and conducted an operating course for members. Income was derived through (1) dues, (2) waste paper sales, (3) the operating course. The

only question in the case was whether the corporation was exempt under Sec. 101 of the income tax law as a business league. The Board of Tax Appeals held that the petitioner was exempt and in the course of its opinion said:

> "There is no doubt but that the petitioner may be classed as a 'business league' for it is an association of members having a common business interest. That common business interest is the betterment of the graphic arts industry in and around Chicago. * * *
>
> "We believe that the avowed purposes of the petitioner, as set forth in the original certificate of incorporation and in Article II of the constitution, were to advance and protect business interests, and thus were those of a business league as that phrase is used in the pertinent section of the statute. * * *
>
> " * * * A careful examination of these facts impels us to the conclusion that any business engaged in by the petitioner 'of a kind ordinarily carried on for profit' was only incidental and subordinate to the main or principal purposes required by statute.' "

Respondent avoids the general rule that a written document is to be interpreted, "taking it by its four corners." As found by the Trial Examiner, petitioner *intended* to form a *business league,* and had no *purpose* to *profit,* neither did it *profit.* No isolated phrase or purely incidental act can upset these facts, and no legal construction can logically be based on the theory of the "tail wagging the dog." The ruling contended for by Petitioner makes legal common sense, the other legal nonsense. The one deals fairly, the other unjustly. Con-

gress must have intended to exempt *business leagues* as *such,* or it would not have attempted to do so. It is entirely rational to assume that any incidental advantage of a *business league* would be reflected in greater income revenue from the *business* benefited.

Petitioner's prayer in its opening brief should be granted.

Respectfully submitted,

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